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Dogfight: Criticizing the Agreement on Subsidies and Countervailing Measures Amidst the Largest Dispute in World Trade Organization History

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Dogfight: Criticizing the Agreement on Subsidies and Countervailing Measures Amidst the Largest Dispute in World Trade Organization History

Cover Page Footnote

International Law; Commercial Law; Law

**Dogfight:
Criticizing the Agreement on Subsidies and
Countervailing Measures Amidst the Largest Dispute
in World Trade Organization History[†]**

ABSTRACT

The United States and the European Union have pointed fingers at each other in the largest dispute in World Trade Organization history. At issue are alleged violations of anti-subsidy provisions regarding aviation titans Boeing and Airbus. The seeds of the feud were planted more than thirty-five years ago when Europe created Airbus to compete with the United States' dominant hold over ninety-four percent of the commercial aircraft market. The current litigation may impact a wide range of individuals: from the nine billion passengers who bought a plane ticket last year, to manufacturing workers in Hamburg, Germany and Everett, Washington. Amidst the multibillion dollar feud, the question must be asked: is the World Trade Organization's Agreement on Subsidies and Countervailing Measures pragmatic? Additionally, can the World Trade Organization's Dispute Settlement Understanding effectively deal with subsidies to large civil aircraft manufacturers? This comment will argue that banning subsidies to the large civil aircraft industry is not practical. Further, the World Trade Organization will not be able to effectively curtail subsidies in the large civil aircraft industry. These arguments are presented along with a brief background, a presentation of the relevant documents, and a forecast of the aviation feud's future.

[†] The author would like to thank his parents, Irving and Marian Lee, for all their support.

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I. Introduction

The feud between aircraft manufacturing giants Airbus and Boeing has soared to the World Trade Organization (WTO)—again. The fight between the world's dominant aviation companies involves countries on both sides of the Atlantic and a

possible four billion dollar slap on the wrist.¹

In October of 2004, the United States and the European Union (EU) initiated the first phase in the WTO Dispute Settlement Understanding (DSU) by requesting consultations.² Both the United States and the European Communities (EC)³ alleged that the other had violated the Agreement on Subsidies and Countervailing Measures (SCM Agreement) by subsidizing Airbus and Boeing, respectively.⁴ These consultations did not resolve the dispute.⁵ Subsequently, on May 31, 2005, the United States initiated the next phase of the DSU by requesting that a panel be formed to investigate its claims.⁶ In response, the European Communities renewed its allegations and requested a panel as well.⁷

On September 23, 2005, the WTO Dispute Settlement Body (DSB) initiated the information-gathering process.⁸ Meanwhile,

¹ Heather Long, *Trade War Fear as WTO Investigates Airbus and Boeing Subsidies*, GUARDIAN (London), July 21, 2005, at 20. Monetary compensation is not part of the DSU; rather, remedies are either a withdrawal of the subsidy, compensation based on mutually agreed trade concessions, or countervailing measures. See discussion on Non-compliance *infra* Part IV.E.

² Request for Consultations by the United States, *European Communities and Certain Member States—Measures Affecting trade in Large Civil Aircraft*, WT/DS316/1 (Oct. 12, 2004) [hereinafter Consultation Request EC—Aircraft]; Request for Consultations by the European Communities, *United States—Measures Affecting Trade in Large Civil Aircraft*, WT/DS317/1 (Oct. 12, 2004) [hereinafter Consultation Request U.S.—Aircraft].

³ For legal reasons, the European Union is referred to as the European Communities in WTO matters. WTO—European Communities, Member Information, http://www.wto.org/english/thewto_e/countries_e/european_communities_e.htm. This comment, however, will use the European Union (EU) and European Communities (EC) interchangeably.

⁴ Consultation Request EC—Aircraft, *supra* note 2; Consultation Request U.S.—Aircraft, *supra* note 2.

⁵ Request for the Establishment of a Panel by the United States, *European Communities and Certain Member States—Measures Affecting Trade in Large Civil Aircraft*, WT/DS316/2 (June 3, 2005) [hereinafter Panel Request EC—Aircraft].

⁶ *Id.*

⁷ Request for the Establishment of a Panel by the European Communities, *United States—Measures Affecting Trade in Large Civil Aircraft*, WT/DS317/2 (June 3, 2005) [hereinafter Panel Request U.S.—Aircraft].

⁸ Agreement on Subsidies and Countervailing Measures annex V(4), Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A,

Britain continued its plan to provide Airbus with £400 million in repayable loans.⁹ This so-called “launch aid” was for the development of a new passenger jet, the A350.¹⁰ Newspapers hyped these events as a catalyst for possibly the “world’s biggest trade war.”¹¹

In February, 2006 the DSB established a panel to hear the dispute.¹² The complexity of the case, however, caused the panel to inform the DSB that it would exceed the WTO’s six month time frame.¹³ The panel, which is the first level of adjudication, is expected to complete its work in 2007.¹⁴

As the United States and European Communities point fingers at each other alleging government subsidy violations, the question must be asked: *is the WTO’s SCM Agreement pragmatic?* This comment will argue that applying the SCM Agreement to special industries, such as large civil aircraft manufacturing, is not practical. The enormous costs in the aircraft manufacturing industry make subsidies necessary. Subsidizing the industry encourages innovation and allows for competition. Thus, the SCM Agreement should not be applied to the civil aircraft industry. Further, the dogfight between the European Communities and United States cannot be resolved successfully using the current WTO resolution process to enforce the SCM Agreement. This is because WTO decisions are enforced by the authorization of trade sanctions by the injured country. Since both countries appear to be guilty of violations and because a trade war is undesirable, enforcement is unlikely.

This comment will unfold in five principle parts. In section II, a brief background of the Airbus-Boeing feud will be presented.

Legal Instruments—Results of the Uruguay Round, *available at* http://www.wto.org/english/docs_e/legal_e/24-scm.pdf [hereinafter SCM Agreement].

⁹ Tracey Boles, *Trade War Looms as UK Grants Aid to Airbus*, BUS., Sept. 18, 2005, at Focus 6.

¹⁰ *Id.*

¹¹ *Id.*

¹² Communication from the Chairman of the Panel, *European Communities and Certain Member States—Measures Affecting Trade in Large Civil Aircraft*, WT/DS316/7 (Apr. 13, 2006).

¹³ *Id.*

¹⁴ *Id.*

Parts III and IV will summarize the relevant legal documents—the SCM Agreement and the DSU. Next, Part V will critique the SCM Agreement and the DSU. Lastly, Part VI will forecast the future scenarios for the aviation feud.

The heart of this paper will cover three areas: an argument against applying the SCM Agreement to large civil aircraft, how the DSU enforcement problem is aggravated when dealing with commercial aviation subsidies, and the future of the dispute. But first, we will visit the beginning.

II. Background on the Aviation Feud

A. *The Arrival of Airbus*

The seeds for the Airbus-Boeing feud were sown a quarter century before the WTO was even formed.¹⁵ In the late 1960s, government-supported British, West German, and French aviation firms began plans to form what was later to become Airbus.¹⁶ Britain left the group in 1969 and did not return until 1979.¹⁷ Thus, Europe's aviation future began as a consortium of France's Aerospatiale and Germany's Deutsche Airbus.¹⁸ Airbus Industrie was officially formed in 1970 and joined by Spain's CASA in 1974.¹⁹ Presently, Airbus is operated through national companies that are each responsible for making specific components.²⁰ Final plane assembly takes place in Toulouse, France and Hamburg, Germany.²¹

¹⁵ The WTO was formed in 1995. WORLD TRADE ORG., THE WORLD TRADE ORGANIZATION 3 (2005), http://www.wto.org/english/res_e/doload_e/inbr_e.pdf (providing and overview of WTO history and structure).

¹⁶ STEPHEN ARIS, CLOSE TO THE SUN: HOW AIRBUS CHALLENGED AMERICA'S DOMINATION OF THE SKIES 223 (2002).

¹⁷ Hans-Joachim Braun, *Innovation in Flight from the Perspective of Europe*, in RECONSIDERING A CENTURY OF FLIGHT 70, 80 (Roger D. Launius & Janet R. Daly Bednarek eds., 2003).

¹⁸ Airbus Corporate Information/People & Organisation/Company Evolution, http://www.airbus.com/en/corporate/people/Airbus_short_history.html (last visited Oct. 17, 2006) [hereinafter Airbus Company Evolution].

¹⁹ *Id.*

²⁰ *Id.*

²¹ Airbus Frequently Asked Questions, <http://www.airbus.com/en/utilities/faqs.html> (click on "Q. Where are Airbus aircraft manufactured?") (last visited Oct. 19,

One of Airbus' initial goals was admittedly to "challenge American supremacy in the aviation industry."²² At Airbus' inception, American aviation firms accounted for ninety-four percent of the commercial airline market.²³ By the late 1990s, however, Airbus had outlasted two of its original heavyweight opponents, McDonnell Douglas²⁴ and Lockheed.²⁵ In 1998, Airbus captured over fifty percent of the global market, beating the world's remaining major manufacturer—Boeing.²⁶

B. U.S. Aviation and Boeing

Boeing Airplane Company is the legacy of William Boeing, who dropped out of Yale to start a successful lumber business.²⁷ After attending the first American Air Meet in 1910, his aviation interest blossomed and six years later he founded Pacific Aero Products.²⁸ A year later in 1917, he changed the company's name to reflect his surname.²⁹

Much of Boeing's history parallels the story of U.S. aviation. The inauguration of human flight took place in 1903 by Americans—the Wright brothers—at Kitty Hawk, North Carolina.³⁰ By World War I, though, the United States was greatly outclassed by European aviation technology.³¹ European governments invested heavily in research and design; this resulted

2006).

²² Airbus Corporate Evolution, *supra* note 18.

²³ Braun, *supra* note 17, at 78-79.

²⁴ ARIS, *supra* note 16, at 225. Boeing bought out McDonnell Douglas in 1996. *Id.*

²⁵ Robert J. Carbaugh & John Olienyk, *Boeing-Airbus Subsidy Dispute: A Sequel*, GLOBAL ECON. J., Dec. 2004, at 2, <http://www.bepress.com/gej/vol4/iss2/6/>. Lockheed exited the commercial airliner market in the early 1980's. *Id.*

²⁶ ARIS, *supra* note 16, at 217. In 2000, Boeing reclaimed an advantage in the market. *Id.*

²⁷ Boeing History—Biographies-Boeing: William E. Boeing, <http://www.boeing.com/history/boeing/boeing.html> (last visited Oct. 17, 2006).

²⁸ Boeing History—The Beginnings: Building a Company, <http://www.boeing.com/history/boeing/building.html> (last visited Sept. 7, 2006).

²⁹ *Id.*

³⁰ Boeing History, *supra* note 27.

³¹ Roger D. Launius, *The Wright Brothers, Government Support for Aeronautical Research, and the Evolution of Flight*, in RECONSIDERING A CENTURY OF FLIGHT 50, 55-56 (Roger D. Launius & Janet R. Daly Bednarek eds., 2003).

in the emergence of the airplane as a battlefield weapon during World War I.³² U.S. aviation manufacturers did not receive major government funding for research and development until World War II, at which time the U.S. aviation industry enjoyed a brief flutter of success.³³ But with the end of World War II came the start of demobilization and a decrease in the level of U.S. government funding for aviation.³⁴ As a result, the post-World War II years saw the U.S. aviation industry struggle, but the struggle was short-lived.³⁵ With the onset of the Cold War, military funding for aerospace research took off and the U.S. industry maintained a steady pulse for the latter half of the twentieth century.³⁶

C. International Trade and Civil Aviation Agreements

Post-World War II international economic relations began at a conference in Bretton Woods, New Hampshire.³⁷ Here, the organizations that later became the World Bank were born.³⁸ Also, the International Monetary Fund was created to facilitate the financial side of European reconstruction.³⁹ Lastly, the International Trade Organization (ITO) was proposed at the conference as a means to regulate trade and reduce tariffs.⁴⁰ The ITO never materialized; however, the General Agreement on Tariffs and Trade (GATT) was created.⁴¹ Originally, GATT was not envisioned as an institution; it was designed as a tool to aid the ITO. In the absence of the ITO, GATT became the main body for international trade until the creation of the WTO.⁴²

GATT was brought into force by twenty-three signatory

³² *Id.* at 55.

³³ *Id.* at 60.

³⁴ *Id.*

³⁵ *Id.* at 61.

³⁶ *Id.* at 61-62.

³⁷ David A. Gantz, *Introduction to the World Trading System and Trade Law protecting U.S. Business*, 18 WHITTIER L. REV. 289, 293 (1997).

³⁸ *Id.*

³⁹ *Id.*

⁴⁰ *Id.*

⁴¹ *Id.*

⁴² *Id.* at 293-94.

countries in 1947.⁴³ It was an attempt to create a framework that would limit tariffs.⁴⁴ The agreement's purpose was to continue liberalizing trade through regular negotiation "rounds."⁴⁵

Originally, GATT did little to dissuade government subsidization. Countries that subsidized products were merely obligated to notify the contracting parties of the extent and ramifications of the subsidization.⁴⁶ If the subsidy prejudiced another country, a discussion about limiting the subsidy would be honored upon request.⁴⁷

In 1955, GATT expanded its agreement on subsidies.⁴⁸ The additions drew distinctions between types of government aid and subsidies.⁴⁹ It also added teeth to enforce the subsidy provision.⁵⁰ Countries were authorized to use countervailing measures against parties that violated the subsidy agreement.⁵¹ Accordingly, tariffs proportional to the subsidized good could be authorized.⁵²

GATT was effective in reducing direct tariffs and its negotiation system produced eight rounds.⁵³ The seventh round took place in Tokyo from 1973 to 1979.⁵⁴ Ninety-nine countries participated in the Tokyo Round, which included, among other things, a plurilateral Agreement on Trade in Civil Aircraft.⁵⁵ The

43 HAMMOND SUDDARDS SOLICITORS, AN ANATOMY OF THE WORLD TRADE ORGANIZATION 1-2 (Konstantinos Adamantopoulos ed., 1997) [hereinafter AN ANATOMY OF THE WTO].

44 Daniel I. Fisher, Note, "*Super Jumbo*" Problem: Boeing, Airbus, and the Battle for the Geopolitical Future, 35 VAND. J. TRANSNAT'L L. 865, 871 (2002).

45 AN ANATOMY OF THE WTO, *supra* note 43, at 2.

46 The General Agreement on Tariffs and Trade, Oct. 30, 1947, 61 Stat. A-3, 55 U.N.T.S. 187 [herein after GATT].

47 *Id.*

48 Shane Spradlin, Comment, *The Aircraft Subsidies Dispute in the GATT's Uruguay Round*, 60 SMU J. AIR L. COM. 1191, 1194 (1995).

49 *Id.* at 1194-95.

50 *See id.* at 1195.

51 *See id.*

52 *Id.*

53 *Id.*

54 Spradlin, *supra* note 48, at 1195.

55 Agreement on Trade in Civil Aircraft, Apr. 12, 1979, GATT B.I.S.D. (26th Supp.) at 162, Annex 4A (1979) [hereinafter Civil Aircraft Agreement].

agreement featured the elimination of all import duties on civil aircraft and components, regulations on government financial support for the industry, and the creation of a Committee on Civil Aircraft.⁵⁶ One criticism was that the term “subsidy” was not specifically defined, but only illustrated by a list of examples.⁵⁷

The eighth GATT round was the birthplace of the WTO. The Uruguay Round began in Punta del Este, Uruguay, but took place mostly at the GATT office in Geneva.⁵⁸ One hundred twenty-five countries participated in the round and it produced the Marrakesh Agreement Establishing the World Trade Organization.⁵⁹ The agreement also annexed significant portions of previous GATT documents.⁶⁰ In all, the Uruguay Round produced eighteen agreements spanning six hundred pages.⁶¹ Relevant to this comment was the unmodified annexation of the Tokyo Round’s Agreement on Trade in Civil Aircraft which has twenty-one signatories.⁶² Another prominent element of the Airbus—Boeing feud—and a major focus of this paper—was the adoption of the SCM Agreement which expanded upon previous negotiations from the Tokyo Round.⁶³

Even with the backdrop of GATT’s success with tariffs, tensions in the air between Europe and the United States were simmering.⁶⁴ In 1984, the United States began negotiations with the hope of extinguishing the types of funding given to Airbus by

⁵⁶ AN ANATOMY OF THE WTO, *supra* note 43, at 26. See Civil Aircraft Agreement, *supra* note 55, at 162.

⁵⁷ Julie Dunne, Note and Comment, *Delverde and the WTO’s British Steel Decision Foreshadow More Conflict Where the WTO Subsidies Agreement, Privatization, and United States Countervailing Duty Law Intersect*, 17 AM. U. INT’L L. REV. 79, 99-100 (2001).

⁵⁸ Gantz, *supra* note 37, at 295.

⁵⁹ Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations, Apr. 15, 1994, 33 I.L.M. 1125 (1994).

⁶⁰ See General Agreements on Tariffs and Trade 1994, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, Legal—Instruments Results of the Uruguay Round, 1867 U.N.T.S. 187, 33 I.L.M. 1144 (1994).

⁶¹ AN ANATOMY OF THE WTO, *supra* note 43, at 6-7.

⁶² *Id.* at 26.

⁶³ *Id.* at 18.

⁶⁴ See Michael J. Levick, Note, *The Production of Civil Aircraft: A Compromise of Two World Giants*, 21 U. DENV. TRANSP. L.J. 434, 441 (1993).

ratcheting up GATT's Agreement on Trade in Civil Aircraft.⁶⁵ As a fall back measure, the United States also pursued informal negotiations outside of GATT; in 1987 the United States and European Union began talks about Airbus' funding.⁶⁶ Although the bilateral negotiations showed some potential, they stalled because the parties could not reach an agreement about the percentage of development costs a government could subsidize.⁶⁷ The stalemate was broken when the United States discovered an explicit German export subsidy to Deutsche Airbus and filed a complaint with the GATT Subsidies Committee.⁶⁸ "[T]he Airbus partner was provided exchange rate guarantees by its government, under the auspices of a privatization program, worth an estimated \$2.5 million on each Airbus aircraft delivered in 1990."⁶⁹ A GATT panel ruled that the German exchange rate guarantee violated the Agreement on Trade in Civil Aircraft.⁷⁰

In the wake of the German exchange rate case, the United States capitalized on its bargaining windfall and finally worked out a bilateral agreement with the European Union.⁷¹ The Agreement Concerning Application of the General Agreement on Tariffs and Trade to Trade in Civil Aircraft (1992 U.S.-E.C. Aircraft Agreement) was signed on July 17, 1992.⁷² The agreement accomplished five notable objectives: (1) future aircraft production subsidies were banned, (2) development subsidies were capped at thirty-three percent of total cost,⁷³ (3) the prohibition of government aviation marketing assistance that grew out of the Tokyo Round was reiterated,⁷⁴ (4) greater disclosure of state support was mandated,⁷⁵ and (5) indirect government support was

⁶⁵ See Spradlin, *supra* note 48, at 1206.

⁶⁶ *Id.* at 1207.

⁶⁷ *Id.*

⁶⁸ *Id.*

⁶⁹ *Id.*

⁷⁰ See Levick, *supra* note 64, at 441.

⁷¹ *Id.*

⁷² Agreement Concerning the Application of the GATT Agreement on Trade in Civil Aircraft on Trade in Larger Civil Aircraft, July 17, 1992, U.S.-E.C., 31 U.S.T. 619.

⁷³ Levick, *supra* note 64, at 452.

⁷⁴ *Id.*

⁷⁵ *Id.* at 456.

limited to three percent of the annual industry sales, and four percent of each company's annual sales.⁷⁶

Despite negotiations and attempts to resolve the subsidy issue, the aviation feud continued. In the fall of 2004, the United States and the European Union attempted to modify the 1992 U.S.-E.C. Aircraft Agreement.⁷⁷ Unfortunately, a new understanding could not be reached and the United States withdrew from negotiations.⁷⁸ Subsequently, the United States turned to the WTO and initiated action pursuant to the SCM Agreement in accordance with the DSU.⁷⁹

III. Agreement on Subsidies and Countervailing Measures (SCM Agreement)

A. Purpose of the SCM Agreement

In the absence of a preamble, the WTO Appellate Body⁸⁰ has relied upon the SCM Agreement's text to ascertain its purpose.⁸¹ The agreement "contains a set of rights and obligations that go well beyond merely applying and interpreting . . . GATT 1947."⁸² Further, "[t]aken as a whole, the main object and purpose of the *SCM Agreement* is to increase and improve GATT disciplines relating to the use of both subsidies and countervailing measures."⁸³

⁷⁶ *Id.* at 457.

⁷⁷ Carbaugh & Olienyk, *supra* note 25, at 3.

⁷⁸ *Id.*

⁷⁹ Panel Request *EC—Aircraft*, *supra* note 5.

⁸⁰ The WTO does not have a per se rule mandating *stare decisis*; however, WTO members rely on past Appellate Body Reports for support and direction. This is understandable considering that the DSU proclaims that the dispute settlement system provides security and predictability. Consequently, this comment has looked to the Appellate Body Reports to help explain WTO agreements. See Valerie Hughes, *WTO Dispute Settlement: An Overview*, in CHALLENGES AND PROSPECTS FOR THE WTO 23, 35 (Andrew D. Mitchell ed., 2005).

⁸¹ Appellate Body Report, *United States—Countervailing Duties on Certain Corrosion-Resistant Carbon Steel Flat Products from Germany*, ¶ 73, WT/DS213/AB/R (Nov. 28, 2002) [hereinafter Appellate Body Report *US—Carbon Steel*].

⁸² Appellate Body Report, *Brazil—Measures Affecting Desiccated Coconut*, ¶ 19, WT/DS22/AB/R (Feb. 27, 1997).

⁸³ Appellate Body Report *US—Carbon Steel*, *supra* note 81.

B. Definition of a Subsidy

The SCM Agreement defines “subsidy” in greater depth than previous GATT agreements had ventured. Under the agreement, a subsidy exists if “there is a financial contribution by a government or any public body within the territory of a Member . . .”⁸⁴ Five instances are provided to define what is meant by “a financial contribution.”

First, a subsidy exists when “a government practice involves a direct transfer of funds (e.g., grants, loans, and equity infusion), potential direct transfers of funds[,] or liabilities (e.g., loan guarantees)[.]”⁸⁵ Second, a subsidy also exists when a government forgoes taxes that would otherwise be due.⁸⁶ Uncollected government revenue that had already accrued before the agreement was exempt from the subsidy prohibition.⁸⁷

Revenue which is “otherwise due” is ambiguous enough to warrant interpretation by the WTO Appellate Body. Theoretically, a government could tax all revenue; therefore, if one took this extreme approach then all governments who did not tax 100% of revenues would fit the subsidy definition. Of course, that would be over-inclusive. “There must, therefore, be some defined normative benchmark against which a comparison can be made between the revenue actually raised and the revenue that would have been raised ‘otherwise.’”⁸⁸

The dispute panel⁸⁹ must determine what a government should be taxing and whether that is consistent with what is actually being taxed. This is not an easy task; each country has a complex tax system and there is no general domestic tax standard that a panel can rely upon.⁹⁰ The WTO Appellate Body has provided guidance: “panels should seek to compare the fiscal treatment of

⁸⁴ SCM Agreement, *supra* note 8, ¶ 1.1(a)(1).

⁸⁵ *Id.* ¶1.1(a)(1)(i).

⁸⁶ *Id.* ¶1.1(a)(1)(ii).

⁸⁷ *Id.* n.1.

⁸⁸ Appellate Body Report, *United States—Tax Treatment for “Foreign Sales Corporations,”* ¶ 90, WT/DS108/AB/R (Feb. 24, 2000) [hereinafter Appellate Body Report *U.S.—FSC*].

⁸⁹ An explanation of the dispute resolution panel will be discussed *infra* Part IV.B.

⁹⁰ See Appellate Body Report *U.S.—FSC*, *supra* note 88, ¶ 91.

legitimately comparable income to determine whether the contested measure involves the foregoing to revenue which is ‘otherwise due’, [sic] in relation to the income in question.”⁹¹

A third instance of subsidization is when a government provides goods or services that are not for the state’s general infrastructure.⁹² A “good” in the SCM Agreement is broad; it includes “tangible items of property, such as trees, that are severable from land.”⁹³ As the Appellate Body observed, a narrow interpretation of a “good” would undermine the agreement.⁹⁴ For example, if a country provided standing trees—a forest—to a lumber enterprise, then a good has been provided; to hold otherwise would open up a detrimental loophole in the agreement.⁹⁵

While the SCM Agreement allows a government to provide support for the “general infrastructure,” that does not mean that government assistance for any infrastructure aid will be tolerated.⁹⁶ The exception only applies to “infrastructure of a *general* nature.”⁹⁷ For example, a government could provide funding for a national oil pipeline, but not a pipeline between an oil refinery and the front door of a manufacturing plant that runs on oil.

Fourth, a subsidy also exists if a government funds a private group that carries out any of the first three instances of subsidies.⁹⁸ This stops governments from circumventing the agreement by using a private entity as a clever mask.

The fifth instance is really a rehash of previous GATT subsidy provisions. A subsidy exists if “there is any form of income or price support in the sense of Article XVI of GATT 1994 and a benefit is thereby conferred.”⁹⁹ Article XVI addresses subsidies

⁹¹ *Id.*

⁹² SCM Agreement, *supra* note 8, ¶1.1(a)(1)(iii).

⁹³ Appellate Body Report, *United States—Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada*, ¶ 59, WT/DS257/AB/R (Jan. 29, 2004) [hereinafter *U.S.—Softwood Lumber IV*].

⁹⁴ *See id.* ¶ 64.

⁹⁵ *See id.*

⁹⁶ *See id.* ¶ 60.

⁹⁷ *Id.* (emphasis in original).

⁹⁸ *Id.* ¶1.1(a)(1)(iv).

⁹⁹ *Id.* ¶1.1(a)(2).

on exports of primary products.¹⁰⁰ A subsidy exists if a government helps to reduce the price of a primary product so that the country can gain more than an equitable share of the world market in that export.¹⁰¹

If one of the five instances of a financial contribution is met, a benefit must also be conferred to a specific enterprise or enterprises for a subsidy to exist. To be considered a conferral of benefit, the recipient must be in a better position after the financial contribution was made than had the contribution not been made at all.¹⁰² The market provides a useful tool in determining whether a "benefit" exists.¹⁰³ "The question whether a 'financial contribution' confers a 'benefit' depends . . . on whether the recipient has received a 'financial contribution' on terms more favourable than those available to the recipient in the market."¹⁰⁴ An enterprise can do business with a government as long as the fair market value is used.¹⁰⁵

The SCM Agreement splits subsidies into three categories: prohibited, actionable, and non-actionable. These three types of subsidies are still under the umbrella of the general definition of subsidy;¹⁰⁶ although each type of subsidy is treated differently by the agreement. The WTO Secretariat analogizes the classification scheme to a traffic light: red is prohibited, yellow is actionable, and green is non-actionable.¹⁰⁷

¹⁰⁰ General Agreement on Tariffs and Trade art. XVI, Oct. 30, 1947, 61 Stat. A-11, 55 U.N.T.S. 194.

¹⁰¹ See WTO SECRETARIAT, GUIDE TO THE URUGUAY ROUND AGREEMENTS 90-91 (1990).

¹⁰² See Appellate Body Report, *Canada—Measures Affecting the Export of Civilian Aircraft*, WT/DS70/AB/R, ¶ 157 (Aug. 2, 1999) [hereinafter *Canada—Aircraft*].

¹⁰³ *Id.*

¹⁰⁴ Appellate Body Report, *United States—Imposition of Countervailing Duties on Certain Hot-Rolled Lead and Bismuth Carbon Steel Products Originating in the United Kingdom*, ¶ 68, WT/DS138/AB/R (May 20, 2000) [hereinafter *U.S.—Lead and Bismuth II*].

¹⁰⁵ See *id.*

¹⁰⁶ Appellate Body Report *U.S.—FSC*, *supra* note 88, ¶ 89 (ruling that the general definition of subsidy applies throughout the SCM Agreement).

¹⁰⁷ WTO SECRETARIAT, *supra* note 101, at 92-97.

C. Prohibited Subsidies

Red light, stop, proceed no further. Prohibited subsidies are those that are more visibly designed to affect trade.¹⁰⁸ These subsidies are “prohibited” because they are more likely to have negative effects on other WTO members.¹⁰⁹ Prohibited subsidies fall into two categories: export subsidies and import substitution subsidies.¹¹⁰

Export subsidies are contingent upon export performance.¹¹¹ Annex I of the SCM Agreement provides a detailed list of export subsidies. These include: (a) direct subsidies to an enterprise based on export performance, (b) currency retention schemes, (c) government mandated internal transportation charges on export shipments that are more favorable to domestic shipments, (d) subsidies on items used for production of exports, (e) tax breaks for export enterprises, (f)-(g) tax deductions directly and indirectly related to exports above those given to products consumed domestically, and (h) indirect taxes on goods or services used in the production of export products.¹¹² Import substitution subsidies are those that are contingent “upon the use of domestic over imported goods.”¹¹³

The SCM Agreement treats prohibited subsidy allegations with a sense of urgency. If a WTO member suspects prohibited subsidies are being provided they can request consultations.¹¹⁴ “[T]he Member believed to be granting or maintaining the subsidy in question shall enter into such consultations as quickly as possible. The purpose of the consultations shall be to clarify the facts of the situation and to arrive at a mutually agreed solution.”¹¹⁵

¹⁰⁸ *Id.* at 93.

¹⁰⁹ *See id.*

¹¹⁰ SCM Agreement, *supra* note 8, ¶ 3.1. An exception is provided in the Agreement on Agriculture. *Id.*

¹¹¹ *Id.* ¶ 3.1(a).

¹¹² *See* SCM Agreement, *supra* note 8, Annex I. Annex I, the list of export subsidies, is over eleven-hundred words long; this summary does not capture all the intricacies of the list. *Id.*

¹¹³ SCM Agreement, *supra* note 8, ¶ 3.1(b).

¹¹⁴ *Id.* ¶ 4.1.

¹¹⁵ *Id.* ¶ 4.3.

Rules for prohibited subsidy allegations are different than those generally applied by the WTO.¹¹⁶ For example, the thirty day consultation period is half as long as those concerning actionable subsidies.¹¹⁷ In general, the deadlines for action on a prohibited subsidy complaint are half as long as regular procedures.¹¹⁸ Also, prohibited subsidy matters can be expedited by the establishment of a five person panel that has expertise in the area in question.¹¹⁹ The expert panel is convened at the behest of the dispute resolution panel;¹²⁰ however, the experts' determination of whether a prohibited subsidy exists must be accepted without modification.¹²¹

If prohibited subsidization is found then the dispute resolution panel immediately recommends that the subsidizing member withdraw the subsidy.¹²² In contrast, actionable subsidies are not given the same sense of urgency; i.e., a finding of actionable subsidies does not mandate an immediate recommendation.¹²³ The appeals process for prohibited subsidies follows the regular DSU system, with the modification of half time-periods.¹²⁴

D. Actionable Subsidies

Actionable subsidies have the cautionary glow of a yellow light; they are not a clear red or green light. As the WTO Secretariat explains, these "are neither prohibited nor exempt from challenge, and which are therefore potentially open to complaint, or to countervailing action, provided the necessary conditions are met."¹²⁵ Whereas prohibited subsidies are absolutely disallowed, actionable subsidies require some analysis to determine if they

¹¹⁶ WTO SECRETARIAT, *supra* note 101, at 94.

¹¹⁷ SCM Agreement, *supra* note 8, ¶ 4.4.

¹¹⁸ *Id.* ¶ 4.12; see also WTO SECRETARIAT, *supra* note 101, at 94.

¹¹⁹ See SCM Agreement, *supra* note 8, ¶ 4.5.

¹²⁰ The dispute resolution panel is explained *infra* Part IV.

¹²¹ SCM Agreement, *supra* note 8, ¶ 4.5.

¹²² *Id.* ¶ 4.7.

¹²³ See *id.* art. 7.

¹²⁴ *Id.* ¶ 4.12.

¹²⁵ WTO SECRETARIAT, *supra* note 101, at 94.

violate the agreement. An actionable subsidy¹²⁶ is one that meets both the general definition of a subsidy¹²⁷ and has an adverse effect on other members.¹²⁸

The possible adverse effects are broken into three categories: “[1] injury to the domestic industry of another Member; [2] nullification or impairment of benefits accruing directly or indirectly to other Members . . . ; [3] serious prejudice to the interest of another Member.”¹²⁹

The injury caused to a government’s domestic industry closely parallels the impact caused by dumping.¹³⁰ Tools for determining an injury to a domestic industry are provided by the SCM Agreement.¹³¹ Two factors are examined in tandem, “both [1] the volume of the subsidized imports and the effects of the subsidized imports on prices in the domestic market for like products and [2] the consequent impact of these imports on the domestic producers of such products.”¹³²

Nullification or impairment occurs when market access by one member is undercut by the effects of another member’s subsidized goods that alter the market.¹³³

The adverse effect of serious prejudice receives great attention

¹²⁶ See SCM Agreement, *supra* note 8, art. 5. There is an agricultural exception per the Agreement on Agriculture. *Id.*

¹²⁷ SCM Agreement, *supra* note 8, art. 1-2. The general definition of a subsidy is discussed *supra* Part III.B.

¹²⁸ SCM Agreement, *supra* note 8, art. 5.

¹²⁹ *Id.*

¹³⁰ WTO SECRETARIAT, *supra* note 101, at 80-81. Dumping occurs when a product is “introduced into the commerce of another country at less than its normal value, if the export price of the product exported from one country to another is less than the comparable price, in the ordinary course of trade, for the like product when destined for consumption in the exporting country.” Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994, April 14, 1994, Multilateral Agreements on Trade and Goods, Annex 1A, Legal Instruments—Results of the Uruguay Round, 33 I.L.M. 81 (1994) [hereinafter Agreement on Implementation of Article VI of GATT].

¹³¹ “The term ‘injury to the domestic industry’ is used here in the same sense it is used in Part V [within Article 15 of the SCM Agreement].” Agreement on Implementation of Article VI of GATT, *supra* note 130, n.11; see SCM Agreement, *supra* note 8, art. 15.

¹³² SCM Agreement, *supra* note 8, ¶ 15.1.

¹³³ WTO SECRETARIAT, *supra* note 101, at 95.

in the SCM Agreement. "[A]n analysis of serious prejudice focuses on situations where a member's export interests are affected by subsidization."¹³⁴ The subsidies are divided into two groups.

In the first group, adverse effects are *presumed* to exist if a subsidy is either: (a) more than 5% of the value of the product, (b) covering operating losses of an industry, (c) covering operating losses by an enterprise, except if it is a one-time part of a long-term solution and it prevents acute social problems, or (d) for the direct forgiveness of debt.¹³⁵ With these four instances the burden is on the member who is being accused.¹³⁶ Previous GATT subsidy agreements did not have these rebuttable presumptions; so, the heavy burden of proving causation has shifted in these four instances.¹³⁷ For any other allegation of serious prejudice, however, the burden is still on the claimant.

In the second group, serious prejudice *may* arise when:

exports from another member into the market of the subsidizing member, or into the market of a third country, are displaced or impeded; [or] significant price undercutting, price suppression or price depression are caused, as compared with sales of a like product of another member in the same market; [or] the subsidized product causes significant loss of sales in the same market; or the subsidy leads to an increase in the subsidizing country's share in the world market for primary product.¹³⁸

If actionable subsidies are found to have adverse effects, remedies have a speedier timetable for dispute resolution than under the normal resolution process.¹³⁹ In terms of urgency, actionable subsidies are somewhere below prohibited subsidies, but above most other matters that go to dispute resolution.¹⁴⁰ The resolution process for actionable subsidies will be discussed later in the DSU discussion.

¹³⁴ *Id.*

¹³⁵ SCM Agreement, *supra* note 8, ¶ 6.1.

¹³⁶ WTO SECRETARIAT, *supra* note 101, at 96.

¹³⁷ *See id.*

¹³⁸ *Id.* at 95.

¹³⁹ *Id.* at 96.

¹⁴⁰ *Id.*

E. Non-actionable Subsidies

With non-actionable subsidies governments have a green light and the most leeway to proceed. Non-actionable subsidies are not a main focus of the aircraft feud; therefore, discussion of these subsidies will be limited. A summary of non-actionable subsidies is: limited assistance for basic research, assistance to disadvantaged regions, and assistance in bringing existing facilities up to speed with environmental regulations.¹⁴¹ Pertinent to the aircraft feud is footnote twenty four of the SCM Agreement, which excludes research on civil aircraft from being considered a non-actionable subsidy.¹⁴²

The SCM Agreement does not provide complete shelter for non-actionable subsidies. A member may request consultations if they believe harmful effects are resulting from the non-actionable subsidies.¹⁴³ Eventually, the committee overseeing the agreement may become involved and make recommendations. A failure to follow recommendations could result in authorization for countermeasures to be taken by the complaining member.¹⁴⁴

F. The Allegations

In their request for a panel, neither the United States nor the European Union included any claims of harmful non-actionable subsidies in their allegations.¹⁴⁵ Both sides of the aircraft feud, however, have alleged prohibited subsidization and actionable subsidization.¹⁴⁶

In its complaint requesting a panel the United States alleged multiple instances of subsidization by the consortium.¹⁴⁷ These included financial contributions for infrastructure and facilities for Airbus companies, forgiveness of debt from launch aid, equity

¹⁴¹ SCM Agreement, *supra* note 8, ¶ 8.2(a)-(c). A list of the limitations and other restrictions are provided in the agreement. *Id.*

¹⁴² *Id.* n.24.

¹⁴³ *Id.* ¶ 9.1.

¹⁴⁴ *Id.* ¶ 9.4.

¹⁴⁵ Panel Request *EC—Aircraft*, *supra* note 5; Panel Request *U.S.—Aircraft*, *supra* note 7.

¹⁴⁶ Panel Request *EC—Aircraft*, *supra* note 5; Panel Request *U.S.—Aircraft*, *supra* note 7.

¹⁴⁷ See Panel Request *EC—Aircraft*, *supra* note 5.

infusions and grants through government controlled banks, and various research and development funding programs.¹⁴⁸ Specifically addressing prohibited subsidies, “[t]he United States is concerned that the launch aid provided by the European Communities and the Member States to Airbus for the development of large civil aircraft . . . appear[s] to be export subsidies inconsistent with [the Prohibited Subsidies article] of the SCM Agreement.”¹⁴⁹ The United States points to development funding programs for the Airbus aircraft models A340-500/600 and the A380.¹⁵⁰ The United States also points to a loan to Airbus’ major parent company from the European Investment Bank.¹⁵¹

In the European Union’s complaint requesting a panel, the European Communities claims that multiple U.S. measures qualify as either prohibited or actionable subsidies. The European Communities alleges state and local government subsidization “through tax breaks, bond financing, lease arrangements, corporate headquarters relocation assistance, research funding, infrastructure measures, and other benefits.”¹⁵² The European Communities alleges such local government subsidization specifically in the states of Washington and Illinois.¹⁵³ Further, the European Communities asserts that NASA, the U.S. Department of Defense, the NIST, and the U.S. Department of Labor have subsidized the aircraft industry with funding and other benefits, including federal income tax incentives.¹⁵⁴

¹⁴⁸ *Id.*

¹⁴⁹ *Id.*

¹⁵⁰ *Id.*

¹⁵¹ *Id.*

¹⁵² Panel Request *U.S.—Aircraft*, *supra* note 7.

¹⁵³ *Id.* Boeing is headquartered in Chicago, IL and has large production facilities in Washington state. Boeing, “Boeing in Brief: About Us,” <http://www.boeing.com/companyoffices/aboutus/brief.html> (last visited Oct. 18, 2006).

¹⁵⁴ See Panel Request *U.S.—Aircraft*, *supra* note 7.

IV. Dispute Settlement Understanding (DSU)

A. Overview

The WTO dispute system¹⁵⁵ will possibly be dealing with the aviation feud for years to come. Nevertheless, the DSU is regarded as an improvement over its predecessor and (relative to other international schemes) is considered a fast-paced mechanism. The WTO Secretariat has explained: “[s]ettling disputes in a timely and structured manner is important. It helps prevent the detrimental effects of unresolved international trade conflicts and mitigates the imbalances between stronger and weaker players by having their disputes settled on the basis of rules rather than having power determine the outcome.”¹⁵⁶ In general, the SCM Agreement accelerates the DSU system’s time frame.¹⁵⁷ In some instances the timetables are cut in half.¹⁵⁸

The WTO dispute resolution system evolved from its GATT predecessor.¹⁵⁹ The GATT system was hampered by several problems. For example, GATT members could delay or block the process by preventing the establishment of a panel.¹⁶⁰ Also, if a panel was formed, a member could hinder the selection of panelists or the term of the panel.¹⁶¹ Further, a decision by the panel could be blocked by the member who was complained against.¹⁶² Even if the panel decision was adopted, GATT

¹⁵⁵ Understanding on Rules and Procedures Governing the Settlement of Disputes, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 2, Legal Texts—The Results of the Uruguay Round of Multilateral Trade Negotiations, 1869 U.N.T.S. 400, 33 I.L.M. 1125 [hereinafter DSU].

¹⁵⁶ WTO SECRETARIAT, A HANDBOOK ON THE WTO DISPUTE SETTLEMENT SYSTEM 1 (2004).

¹⁵⁷ *Id.* at 61. For example, the SCM Agreement calls for a swifter approach for actionable and prohibited subsidies. *Id.*

¹⁵⁸ For example, the Appellate Body in the DSU system should submit their report to the DSB within thirty days under the SCM Agreement, but in regular cases a sixty day window is opened. See DSU, *supra* note 155, art. 17.5; SCM Agreement, *supra* note 8, ¶ 4.9.

¹⁵⁹ Peter Lichtenbaum, *Procedural Issues in WTO Dispute Resolution*, 19 MICH. J. INT’L L. 1195, 1198 (1998).

¹⁶⁰ *Id.* at 1199.

¹⁶¹ *Id.*

¹⁶² *Id.*

members could not be certain that countervailing measures would be authorized in the event of non-compliance.¹⁶³ The result of this inefficiency was a sweeping overhaul of reforms during the Uruguay Round.¹⁶⁴

Piloting the DSU is the Dispute Settlement Body (DSB). The DSB is entrusted with "the authority to establish panels, adopt panel and Appellate Body reports, maintain surveillance of implementation of rulings and recommendations, and authorize suspension of concessions and other obligations under the covered agreements."¹⁶⁵ This single body responsible for dispute resolution is another improvement over GATT.¹⁶⁶ Previously, separate committees oversaw each different agreement resulting in forum shopping.¹⁶⁷ The unified administration of the DSU streamlines the process and eliminates forum shopping.

The DSB is composed of representatives of all WTO members.¹⁶⁸ Their decisions are decided by a consensus; a proposed matter passes if no member present makes an affirmative objection.¹⁶⁹ For matters concerning plurilateral trade agreements, such as the Agreement on Trade in Civil Aircraft, the only members who participate are those who represent a party to the plurilateral agreement.¹⁷⁰

B. Litigation

Currently, the WTO dispute resolution process starts with bilateral talks. As with any type of litigation, ending it before it starts is preferred. U.S. trade representative, Rob Portman and his European counterpart, Peter Mandelson, have stated their preference would be to negotiate rather than to litigate the aviation

¹⁶³ *See id.*

¹⁶⁴ *See id.* at 1200-01.

¹⁶⁵ DSU, *supra* note 155, art. 2.1.

¹⁶⁶ *See* David Palmeter, *The WTO as a Legal System*, 24 FORDHAM L. REV. 444, 469 (2000), *reprinted in* DAVID PALMETER, *WTO AS A LEGAL SYSTEM: ESSAYS ON INTERNATIONAL TRADE LAW AND POLICY* 305, 328 (2003).

¹⁶⁷ *Id.*

¹⁶⁸ WTO SECRETARIAT, *supra* note 156, at 17.

¹⁶⁹ DSU, *supra* note 155, n.1.

¹⁷⁰ *See id.*, art. 2.1.

subsidy dispute.¹⁷¹

Similar to the GATT system, the DSU begins with a consultation stage.¹⁷² The hope is that consultations will yield a solution and avoid litigation.¹⁷³ In most instances, however, parties have already extensively negotiated informally before consultations are requested.¹⁷⁴ In fact, the negotiations to modify the 1992 U.S.-E.C. Aircraft Agreement precipitated the consultation request.¹⁷⁵ The majority of disputes do not move past the consultation stage; they are either settled or the complainant does not continue for other reasons.¹⁷⁶

If these “consultations” fail, then a “panel” is established to resolve the dispute.¹⁷⁷ In the instant aviation dispute, additional consultations were requested by the European Union after a panel was requested.¹⁷⁸ The European Union wanted to clarify statements made by the United States at the DSB meeting following the request for a panel.¹⁷⁹ The additional consultations caused a delay but a panel was eventually formed.

In contrast to the GATT era, a WTO member’s request for the establishment of a panel is virtually assured to be honored.¹⁸⁰ Also, the SCM Agreement expedites the normal process and does not allow a member’s objection to delay the formation of a panel.¹⁸¹ Since there is no permanent panel, the DSB creates a

¹⁷¹ See Ameet Sachdev, *U.S., EU Ease Plane Stances; Sides Willing to Talk on Government Aid*, CHI. TRIB. Oct. 11, 2005, §3 at 3.

¹⁷² See David Palmeter, *National Sovereignty and the World Trade Organization*, 2 J. WORLD INTELL. PROP. 77, 80 (2000), reprinted in DAVID PALMETER, *WTO AS A LEGAL SYSTEM: ESSAYS ON INTERNATIONAL TRADE LAW AND Policy* 259, 262 (2003).

¹⁷³ *Id.*

¹⁷⁴ *Id.*

¹⁷⁵ See *supra* notes 77-79 and accompanying text.

¹⁷⁶ WTO SECRETARIAT, *supra* note 156, at 43-44.

¹⁷⁷ See DSU, *supra* note 155, art. 4-6.

¹⁷⁸ Request for Consultations by the European Communities, *United States—Measures Affecting the Trade in Large Civil Aircraft Addendum*, WT/DS317/1/Add.1 (July 1, 2005).

¹⁷⁹ *Id.*

¹⁸⁰ See WTO SECRETARIAT, *supra* note 156, at 49; DSU, *supra* note 155, art. 6.

¹⁸¹ See SCM Agreement, *supra* note 8, ¶ 4.4; WTO SECRETARIAT, *supra* note 156, at 61.

new three-person¹⁸² panel for every dispute.¹⁸³ The DSU details qualifications for the panelists, including experience¹⁸⁴ and independence from the dispute.¹⁸⁵

During the selection process the WTO Secretariat proposes nominations for the panel to the parties.¹⁸⁶ Parties may reject a panelist nominee. A party, however, cannot indefinitely stall the proceedings by perpetually rejecting nominees. If the parties cannot agree on panelists within twenty days after the establishment of a panel, either party may request intervention.¹⁸⁷ The Director-General, in consultation with the chairpersons of the DSB and the relevant committee or council, will choose the panelists.¹⁸⁸

The time frame for panel selection is compressed when dealing with subsidies. Under the SCM Agreement, the composition of the panel should be finalized fifteen days after the panel is established.¹⁸⁹ For prohibited subsidies, the panelists should immediately be selected.¹⁹⁰

The aviation feud has not followed these fast paced timetables. As some journalists predicted, delays were incurred as the United States and European Union could not agree on panelists.¹⁹¹ In an interesting twist, Director-General Pascal Lamy recused himself from appointing panelists because of his former position as European Union trade commissioner.¹⁹² Instead, one of Lamy's

¹⁸² "Panels shall be composed of three panelists unless the parties to the dispute agree, within 10 days from the establishment of the panel, to a panel composed of five panelists. Members shall be informed promptly of the composition of the panel." DSU, *supra* note 155, art. 8.5.

¹⁸³ WTO SECRETARIAT, *supra* note 156, at 50.

¹⁸⁴ See DSU, *supra* note 155, art. 8.1.

¹⁸⁵ See *id.* art. 8.2.

¹⁸⁶ *Id.* art. 8.6.

¹⁸⁷ See DSU, *supra* note 155, art. 8.7.

¹⁸⁸ See *id.*

¹⁸⁹ SCM Agreement, *supra* note 8, ¶ 7.4.

¹⁹⁰ *Id.*, ¶ 4.4.

¹⁹¹ See *Flying Test*, FIN. TIMES (London- Asia Ed. 1), Aug. 9, 2005, Observer, at 10.

¹⁹² See, e.g., Alan Beattie, *Lamy Waives right to Name WTO Panel*, FIN. TIMES (London), Oct. 8, 2005, § World News, at 9.

deputies made the selections.¹⁹³

The panel functions as the first stage in litigation. As the WTO Secretariat explains: “Panels are the quasi-judicial bodies, in a way tribunals, in charge of adjudicating disputes between members in the first instance.”¹⁹⁴ The panel’s most important role is to submit a report to the WTO members.¹⁹⁵ A panel report issued to the members of the WTO will not become binding until it is adopted by the DSB.¹⁹⁶

Recently, to increase confidence and transparency in the system, disputing members have agreed to open up hearings to the public.¹⁹⁷ In the instant dispute, both parties have agreed to open the proceedings to the public and so the public will access the hearings for what is only the second time in WTO dispute resolution history.¹⁹⁸

C. Appeals

Panel decisions may be appealed to the Appellate Body.¹⁹⁹ The Appellate Body, unlike the panels, is made up of permanent members.²⁰⁰ The seven members are appointed by a consensus of the DSB for four year terms and can be reappointed once.²⁰¹ The members are not affiliated with any government, however their backgrounds represent the diverse membership of the WTO.²⁰² The current members of the Body are nationals of Egypt, Brazil, India, the United States, South Africa, Italy, and Japan.²⁰³

Issues before the Appellate Body “shall be limited to issues of law covered in the panel report and legal interpretations developed

¹⁹³ *Id.*

¹⁹⁴ WTO SECRETARIAT, *supra* note 156, at 21.

¹⁹⁵ *See id.*

¹⁹⁶ WTO SECRETARIAT, *supra* note 156, at 61.

¹⁹⁷ *See* Aimee Turner, *Doors to WTO Trade Dispute Hearings to be Thrown Open*, FLIGHT INT’L, Jan. 24, 2006, at 5.

¹⁹⁸ *Id.*

¹⁹⁹ *See* DSU, *supra* note 155, art. 17.

²⁰⁰ *Id.*, art. 17.1.

²⁰¹ *Id.*, art. 17.2.

²⁰² *See id.*

²⁰³ WTO Dispute Settlement–Appellate Body Members, http://www.wto.org/english/tratop_e/dispu_e/ab_members_descrp_e.htm.

by the panel.”²⁰⁴ Consequently, questions of fact are laid to rest in the panel stage.

If the appeal fails and the member still refuses to comply with the penalty, then the injured member may be authorized to enact countervailing measures (self-help).²⁰⁵

D. Implementation

The DSU stresses the importance of implementation: “Prompt compliance with recommendations or rulings of the DSB is essential in order to ensure effective resolution of disputes to the benefit of all Members.”²⁰⁶

In the event of a successful violation complaint the implementation phase follows. After adoption of a panel or Appellate Body report, a meeting will be held within thirty days.²⁰⁷ The concerned member will announce its intentions with respect to implementation of the DSB recommendations and rulings.²⁰⁸ Also, this meeting is usually used to address the time-period for implementation.²⁰⁹

The concerned member is required to immediately comply with recommendations and rulings, unless it is impractical to do so.²¹⁰ If a member cannot comply immediately, they are given a “reasonable period of time.”²¹¹ This reasonable period of time cannot delay the implementation past fifteen months starting from the establishment of the panel stage.²¹² This time cap can be extended by the DSB to eighteen months, or longer if the parties agree that there are exceptional circumstances.²¹³ Notably, the SCM Agreement does not observe a reasonable period of time for

²⁰⁴ DSU, *supra* note 155, art. 17.6.

²⁰⁵ *See id.*, art. 22.

²⁰⁶ DSU, *supra* note 155, art. 21.1.

²⁰⁷ *Id.*, art. 21.3.

²⁰⁸ *Id.*

²⁰⁹ WTO SECRETARIAT, *supra* note 156, at 76.

²¹⁰ DSU, *supra* note 155, art. 21.3.

²¹¹ *Id.*

²¹² *Id.*, art. 21.4.

²¹³ *Id.*

prohibited subsidization.²¹⁴ Rather, at the panel stage the panelists must recommend immediate withdrawal and a specific time frame for this to happen.²¹⁵

The DSB will continue to monitor the implementation of the recommendations and rulings.²¹⁶ Further, any member may raise the issue of implementation at any time.²¹⁷ The specific issue and its implementation will be included on the DSB meeting agenda until the subsidy is resolved.²¹⁸ As long as the subsidy issue lingers, it remains under surveillance even if measures have been taken for non-compliance.²¹⁹

E. Non-compliance

In the event that a losing member is required to take action and simply does nothing, non-compliance is easy to identify. The issue of identifying non-compliance becomes cloudier when the losing member passes a new law or regulation with the belief that it satisfies the recommendations and ruling.²²⁰ When members disagree as to whether there is compliance or not, the matter is referred to a panel by the DSB.²²¹ Whenever possible, this panel is made up of the persons on the original panel.²²² A report from the panel will be produced within ninety days of the referral of the matter.²²³ Although the DSU does not explicitly state that the compliance panel report can be appealed, it is allowed and frequently done.²²⁴

If the “reasonable period of time” expires, and the losing

²¹⁴ See SCM Agreement, *supra* note 8, ¶ 4.7.

²¹⁵ *Id.*

²¹⁶ DSU, *supra* note 155, art. 21.

²¹⁷ *Id.* art. 21.6.

²¹⁸ The issue is mandated to appear on the agenda six months after the establishment of a reasonable period of time for implementation. At least ten days before each meeting the concerned members must submit a written report of its progress. *See id.*

²¹⁹ See DSU, *supra* note 155, art. 22.8.

²²⁰ See WTO SECRETARIAT, *supra* note 156, at 79.

²²¹ See DSU, *supra* note 155, art. 21.5.

²²² *See id.*

²²³ In the event that the panel cannot produce the report within ninety days, the panel will explain this to the DSB in writing. *See id.*

²²⁴ See WTO SECRETARIAT, *supra* note 156, at 79.

member has not conformed to the recommendations and rulings, temporary measures are available to the prevailing member.²²⁵ These measures provide negotiations where the non-implementing member and prevailing member will attempt to agree upon compensation.²²⁶ This compensation is not a cash pay-off; rather, it is a benefit such as a tariff reduction offered to the prevailing member.²²⁷ Partly because compensation is voluntary,²²⁸ mutually agreed-upon compensation solutions rarely are made.²²⁹

If, within twenty days after the "reasonable period of time" has passed, no compensation solution is reached, the most serious consequence may occur.²³⁰ The prevailing member "may request authorization from the DSB to suspend the application to the Member concerned of concessions or other obligations under the covered agreements."²³¹ These sanctions are referred to by the SCM Agreement as "countervailing measures."²³²

Prohibited subsidies, under the SCM Agreement, bypass the twenty day compensation negotiations and proceed with countervailing measures immediately.²³³ In the event of actionable subsidies, the prevailing member may request countermeasures for non-compliance six months after the DSB adopts either the Appellate Body or panel report.²³⁴

The rules for retaliation are complex and detailed. Generally, the countermeasures taken must be in proportion to the harm caused to the prevailing member.²³⁵ For example, if a subsidy causes four billion euros worth of harm to another member's civil aircraft industry, then a hundred billion euro tariff surcharge

²²⁵ See DSU, *supra* note 155, arts. 3.7 & 22.1.

²²⁶ See DSU, *supra* note 155, art. 22.2.

²²⁷ See WTO SECRETARIAT, *supra* note 156, at 80.

²²⁸ See DSU, *supra* note 155, art. 22.1.

²²⁹ See WTO SECRETARIAT, *supra* note 156, at 80.

²³⁰ See DSU, *supra* note 155, art. 22.2.

²³¹ *Id.*, art. 22.2.

²³² See SCM Agreement, *supra* note 8.

²³³ Unless the DSB decides by consensus to reject the request for countervailing measures, which would require the prevailing party to sit by and do nothing, the request is virtually guaranteed. See SCM Agreement, *supra* note 8, ¶ 4.10.

²³⁴ *Id.*, ¶ 7.9.

²³⁵ DSU, *supra* note 155, art. 22.3.

would be an inappropriate countermeasure. In addition, the sanctions must correspond to the sector harmed.²³⁶ For example, countermeasures for a patent violation should relate to patents.²³⁷

If the parties cannot agree on the complainant's request for retaliation, then arbitration can be requested.²³⁸ The arbitrators²³⁹ should be the original panelists, if available; if they are not available the WTO Director-General shall make a selection.²⁴⁰ During this type of arbitration, sanctions are halted and the arbitrators determines whether the prevailing member's proposed countermeasures are proportional to the trade harm inflicted.²⁴¹

F. Dispute Resolution in Practice

Compared to GATT, the WTO has proven to be successful. There are, however, several cases that expose the weaknesses in the current DSU system. The Banana Wars and the foreign sales corporation scheme are presented to illustrate the complexity of resolving a dispute when opposing members tenaciously resist. Also, the Canada-Brazil aviation feud is discussed as a parallel case to the current dispute, which may serve as the clearest window into the future.

In *European Communities—Regime for the Importation, Sale and Distribution of Bananas (EC—Bananas)*, the DSU failed.²⁴² The complainants alleged that former European colonies were shown favorable treatment through tariff preferences, specifically with regard to banana imports.²⁴³ The dispute proceeded through consultations,²⁴⁴ the panel stage,²⁴⁵ appellate review,²⁴⁶ arbitration

²³⁶ *Id.*, art. 22.3(d)(i).

²³⁷ See WTO SECRETARIAT, *supra* note 156, at 82.

²³⁸ DSU, *supra* note 155, art. 22.6.

²³⁹ The "arbiter" in the DSU refers to either individuals or a group. DSU, *supra* note 155, n.15.

²⁴⁰ *Id.*, art. 22.6.

²⁴¹ WTO SECRETARIAT, *supra* note 156, at 84.

²⁴² Notification of Mutually Agreed Solution, *European Communities—Regime for the Importation, Sale and Distribution of Bananas*, WT/DS27/58 (July 2, 2001).

²⁴³ See Panel Report, *European Communities- Regime for the Importation, Sale, and Distribution of Bananas*, IV, ¶ 9, WT/DS27/R/ECU (May 22, 1997).

²⁴⁴ Request for Consultations by Guatemala, Honduras, Mexico, and the United States, *European Communities—Regime for the Importation, Sale and Distribution of*

concerning implementation,²⁴⁷ and appeal of the arbiter's report²⁴⁸ before a mutually agreed upon solution was reached.²⁴⁹ But the mutually agreed-upon solution did not resolve the dispute. These so-called "Banana Wars" began in the early 1990s, before the WTO was formed, and continue to this day.²⁵⁰ Along the way, the United States began countervailing measures five months before the WTO actually gave authorization.²⁵¹

As the European Union resisted the DSU system, the WTO ruled on a different U.S.-E.C. dispute, which impacted the Banana War. In *United States—Tax Treatment for "Foreign Sales Corporations" (U.S.—FSC)*, the European Union prevailed in a complaint against the United States.²⁵² This ruling provided the European Union with leverage.²⁵³ The result was a bilateral agreement; a settlement which included a new EU tariff system due by 2006.²⁵⁴ The agreement has not signaled an end to the

Bananas, WT/DS16/1 (Oct. 4, 1995) [hereinafter Request for Consultations *EC—Bananas*].

²⁴⁵ Panel Report, *European Communities—Regime for the Importation, Sale and Distribution of Bananas*, WT/DS27/R/ECU, WT/DS27/R/GTM, WT/DS27/R/HND, WT/DS27/R/MEX, WT/DS27/R/USA (May 22, 1997).

²⁴⁶ Appellate Body Report, *European Communities—Regime for the Importation, Sale and Distribution of Bananas*, WT/DS27/AB/R (Sept. 9, 1997).

²⁴⁷ Arbitration of the Understanding on Rules and Procedures Governing the Settlement of Disputes Award of the Arbitrator Said El-Naggar, *European Communities—Regime for the Importation, Sale and Distribution of Bananas*, WT/DS27/15 (Jan. 7, 1998).

²⁴⁸ Recourse to Arbitration by the European Communities Under Article 22.6 of the DSU, *European Communities—Regime for the Importation, Sale and Distribution of Bananas*, WT/DS27/ARB/ECU (Apr. 9, 1999).

²⁴⁹ See Notification of Mutually Agreed Solution, *supra* note 242.

²⁵⁰ See Raj Bhala, *The Banana War*, 31 McGEORGE L. REV. 839, 848-50 (2000).

²⁵¹ See *id.* at 941-43.

²⁵² Second Recourse to Article 21.5 of the DSU by the European Communities, *United States—Tax Treatment for "Foreign Sales Corporations,"* WT/DS108/RW2 (Sept. 30, 2005) [hereinafter Second Recourse *EC—FSC*].

²⁵³ Hunter R. Clark, Amy Bogan & Hayley Hanson, *The WTO Ruling on Foreign Sales Corporations: Costliest Battle Yet in an Escalating Trade War Between the United States and the European Union?*, 10 MINN. J. GLOBAL TRADE 291, 315-16 (2001).

²⁵⁴ Amelia Porges, *Settling WTO Disputes: What do Litigation Models Tell Us?*, 19 OHIO ST. J. ON DISP. RESOL. 141, 164 n.85 (2003). The tariff promise threatened the next GATT/WTO Round. Certain countries refused to launch the Doha Rounds until they received waivers from the yet to be created new tariff system. *Id.*

Banana War. As of the writing of this comment, the WTO is still metaphorically slipping on bananas. EU proposals for a new tariff system have been rejected twice.²⁵⁵ Considering that Guatemala, Honduras, Mexico and the United States²⁵⁶ initiated the consultation stage in September of 1996, the Banana Wars have haunted the WTO for most of its history.²⁵⁷

Not only did *U.S.—FSC* send ripples through the Banana War, it is also an example of the DSU system's lack of results. Like *EC—Bananas*, *U.S.—FSC* ran the gamut of the DSU stages.²⁵⁸ The dispute began brewing in the 1970s when the United States implemented a tax scheme to remedy its losses in the world export battle.²⁵⁹

The United States created the Foreign Sales Corporation (FSC) tax scheme as part of the Deficit Reduction Act of 1984.²⁶⁰ U.S. parent corporations were given tax breaks on foreign trade income (dividends) earned from international subsidiaries acting as the exporters.²⁶¹ This scheme was rejected by the DSB as a violation of several international agreements including the SCM Agreement.²⁶²

Following its loss on appeal in 2000,²⁶³ the United States repealed the FSC tax scheme, but replaced it with the ETI Act, which also failed to receive DSB approval.²⁶⁴ In 2003, the

²⁵⁵ WTO—Dispute Settlement—the disputes-DS27, http://www.wto.org/english/tratop_e/dispu_e/cases_e/ds27_e.htm (summarizing the conflict to date) (last updated Oct. 9, 2006).

²⁵⁶ Ecuador joined in after it became a member of the WTO. See Request for Consultations by Ecuador, Guatemala, Honduras, Mexico, and the United States, *European Communities—Regime for the Importation, Sale and Distribution of Bananas*, WT/DS27/1 (Feb. 5, 1996).

²⁵⁷ Request for Consultations *EC—Bananas*, *supra* note 244.

²⁵⁸ See Second Recourse *EC—FSC*, *supra* note 252, ¶ 1.1.

²⁵⁹ James Joseph Shallue, *An Analysis of Foreign Sales Corporations and the European Communities' Four Billion-Dollar Retaliation*, 31 DENV. J. INT'L L. & POL'Y 179, 180 (2002).

²⁶⁰ Pub. L. No. 98-369, 98 Stat. 494 (1984). The parts relating to FSCs were codified in I.R.C. §§ 921-927 (1984).

²⁶¹ See Second Recourse *EC—FSC*, *supra* note 252, ¶¶ 2.4, 2.5.

²⁶² See Shallue, *supra* note 259, at 181.

²⁶³ See *id.* at 204-05.

²⁶⁴ See *id.*

European Union was authorized to impose four billion dollars in sanctions.²⁶⁵ The European Union, however, stated that it would not implement countermeasures so long as the U.S. Congress was trying to comply.²⁶⁶ The United States jettisoned the ETI Act but replaced it with a parachute: the American Jobs Creation Act of 2004.²⁶⁷ In the fall of 2005 the DSB compliance panel rejected the Jobs Act.²⁶⁸ Both the ETI and Jobs Act clung to the FSC tax scheme through “grandfather” and “transitional” clauses.²⁶⁹ The United States appealed the compliance panel decision and lost.²⁷⁰

Both *EC—Bananas* and *U.S.—FSC* are examples of the DSU producing no results. Despite the threat of using authorized sanctions and even the diligent use of countervailing measures, WTO members can still thwart compliance. Alternatively, when adversaries are both guilty they may choose to allow no result. This was the case in the Canada-Brazil aircraft dispute.

Canada and Brazil provide the only previous large civil aircraft dispute brought before the DSB. Like the instant dispute, the members both alleged that the other was subsidizing their respective aviation industries in violation of the SCM Agreement. In *Brazil—Export Financing Programme for Aircraft (Brazil—Aircraft)*, Canada claimed Brazil’s *Programa de Financiamento às Exportações* (PROEX) violated the SCM Agreement.²⁷¹ The Brazilian subsidy program supported its national aviation champion, *Empresa Brasileira de Aeronautica S.A. (Embraer)*.²⁷² PROEX reduced the cost of aircraft purchases for buyers.²⁷³ The

²⁶⁵ Recourse by the European Communities to Article 4.10 of the SCM Agreement and Article 22.7 of the DSU, *United States—Tax Treatment for “Foreign Sales Corporations,”* WT/DS108/26 (Apr. 25, 2003).

²⁶⁶ *Id.* at 213.

²⁶⁷ See Second Recourse *EC—FSC*, *supra* note 252, ¶ 2.14.

²⁶⁸ *Id.*, ¶ 8.1.

²⁶⁹ See *id.*, ¶¶ 2.12, 2.17.

²⁷⁰ Appellate Body Report and Panel Report pursuant to Article 21.5 of the DSU, *United States Tax Treatment for Foreign Sales Corporations*, WT/DS108/36 (Mar. 17, 2006).

²⁷¹ Request for Consultation by Canada, *Brazil—Export Financing Programme for Aircraft*, WT/DS46/1 (June 21, 1996).

²⁷² See Ivan Krmpotic, *Brazil—Aircraft: Qualitative and Temporal Aspects of “Withdrawal” Under SCM Article 4.7*, 33 LAW & POL’Y INT’L BUS. 653, 659 (2002).

²⁷³ *Id.* (quoting in part Panel Report, *Brazil—Export Financing Programme for*

government agreed to subsidize part of the loans buyers took out to pay for Embraer planes.²⁷⁴ Brazil would pay 3.8 percentage points of the interest rate to the bank via national treasury bonds; the buyer was responsible for the rest of the loan.²⁷⁵ The DSB found that this practice was a prohibited subsidy under the SCM Agreement and recommended withdrawal.²⁷⁶

Compliance with the DSB report became an issue because “withdrawal” of the PROEX subsidy was unclear. Brazil claimed that it could continue to issue the treasury bonds for the buyer agreements that were made before the DSB ruling.²⁷⁷ Eventually, the compliance panel and the Appellate Body ruled against Brazil.²⁷⁸ Subsequently, in late 2000, Canada was authorized to impose countervailing measures to the tune of C\$344.2 million (US \$233.5 million) a year.²⁷⁹ These sanctions have not been imposed because of Brazil’s subsequent successful WTO litigation against Canada; this litigation can be analogized to a counterclaim.

In *Canada—Measures Affecting the Export of Civilian Aircraft*, Brazil accused Canada of subsidizing its national aviation champion, Bombardier, Inc. (Bombardier).²⁸⁰ The panel found prohibited subsidization under the SCM Agreement.²⁸¹ After an unsuccessful appeal, Canada implemented the DSB’s recommendations.²⁸² Brazil challenged the sufficiency of Canada’s compliance, but lost in July of 2000.²⁸³ This, however,

Aircraft, WT/DS46/R (Apr. 14, 1999)).

²⁷⁴ See *id.*

²⁷⁵ *Id.*

²⁷⁶ Appellate Body Report, *Brazil—Export Financing Programme for Aircraft Recourse by Canada to Article 21.5 of the DSU*, ¶ 82(b), WT/DS46/AB/RW (July 21, 2000).

²⁷⁷ See Krmpotic, *supra* note 272, at 665-67.

²⁷⁸ See *id.* at 668.

²⁷⁹ See Panel Report, *Brazil—Export Financing Programme for Aircraft Second Recourse by Canada to Article 21.5 of the DSU*, ¶ 1.6, WT/DS46/RW/2 (July 26, 2001).

²⁸⁰ *Canada—Aircraft*, *supra* note 102, ¶ 2.

²⁸¹ Panel Report, *Canada—Measures Affecting the Export of Civilian Aircraft*, ¶ 10.1, WT/DS70/R (Apr. 14, 1999).

²⁸² Appellate Body Report, *Canada—Measures Affecting the Export of Civilian Aircraft Recourse by Brazil to Article 21.5 of the DSU*, ¶ 4, WT/DS70/AB/RW (July 21, 2000).

²⁸³ WTO—Dispute Settlement—the disputes-DS70, <http://www.wto.org/english/>

was not the end to Brazil's fight.

Canada—Export Credits and Loan Guarantees for Regional Aircraft would supply Brazil with a counterweight for the sanctions from *Brazil—Aircraft*. In January of 2001, consultations with Canada were requested.²⁸⁴ The allegations included (among other things) claims that loan guarantees violated the SCM Agreement.²⁸⁵ In the panel stage, Brazil prevailed; Canadian account financing to Air Wisconsin, Air Nostrum, and Comair were prohibited subsidies.²⁸⁶ In May of 2002, Brazil sought permission to use countervailing measures.²⁸⁷ They claimed Canada had failed to implement the DSB's recommendations and rulings within the mandatory ninety-day period.²⁸⁸ Brazil was successful again; the arbiter authorized sanctions up to US \$247,797,000.²⁸⁹ As of the writing of this comment, these sanctions have not been implemented.

The Canada-Brazil aviation dispute exposed definitive violations of the SCM Agreement, but yielded no results because neither member was interested in sparking a trade war. Consequently, they continued to subsidize their respective industries and did not use the countervailing measures granted by the DSB.²⁹⁰ Similarly, the U.S.-E.C. aviation dispute involves possible subsidy activities on both sides. In light of the Canada-Brazil dispute and the nature of the large civil aircraft industry, it is clear that the DSU will not likely be able to enforce the SCM

tr atop_e/dispu_e/cases_e/ds70_e.htm (summarizing the dispute to date) (last updated Oct. 9, 2006).

²⁸⁴ Request for Consultations by Brazil, *Canada—Export Credits and Loan Guarantees for Regional Aircraft*, WT/DS222/1 (Jan. 25, 2001).

²⁸⁵ See *id.*

²⁸⁶ Panel Report, *Canada—Export Credits and Loan Guarantees for Regional Aircraft*, ¶ 8.1, WT/DS222/R (Jan. 28, 2002).

²⁸⁷ See Recourse to Arbitration by Canada under Article 22.6 of the DSU and Article 4.11 of the SCM Agreement, *Canada—Export Credits and Loan Guarantees for Regional Aircraft*, ¶ 1.2, WT/DS222/ARB (Feb. 17, 2003) [hereinafter *Recourse to Arbitration Canada—Aircraft Credits and Loans*].

²⁸⁸ See *id.*, ¶ 1.1.

²⁸⁹ Recourse to Arbitration *Canada—Aircraft Credits and Loans*, *supra* note 287, ¶ 4.1.

²⁹⁰ See Edward Alden & Raphael Minder, *War of Aircraft Titans gives WTO Biggest Case*, FIN. TIMES (London), June 1, 2005, § International Economy, at 8.

Agreement in the instant dispute.

VI. Criticisms of the SCM Agreement and DSU

A. *Problems with the SCM Agreement*

At the heart of the aircraft dispute is the SCM Agreement. The drafters specifically had large civil aircraft in mind. A footnote under non-actionable subsidies singles out the commercial aviation industry to exclude it from an exception provision.²⁹¹ This comment argues that the agreement, as applied to large civil aircraft, is not practical. The SCM agreement cannot be practically applied to the Airbus-Boeing dispute because the agreement presupposes that subsidies are inherently bad for trade. The civil aircraft industry is simply a different creature. Notably, this paper does not argue against the general application of the SCM Agreement. In fact, the agreement, when applied to most products, allows for innovation and competition. The enormous cost involved with manufacturing large planes alters the paradigm for viewing subsidies. Prohibiting subsidization of the large civil aircraft industry (i) stifles innovation, (ii) discourages competition, and (iii) is unrealistic.

B. *Stifling Innovation*

The sky high cost of designing new aircraft makes modernization an expensive process. While this comment asserts that both Airbus and Boeing receive subsidies, the benefits on the EU side are greater than those on the U.S. side. The financial support behind Airbus has allowed it to be considerably more innovative. For instance, over a ten year period, launch aid has allowed Airbus to develop five new planes, while Boeing has only been able to afford one.²⁹² As a former Boeing chief executive complained, Airbus could afford to gamble with new designs because the risk was on the taxpayers.²⁹³ A curator for the National Air and Space Museum, Smithsonian Institution, explained that “[a]erospace manufacturers literally bet the

²⁹¹ See *supra* note 142 and accompanying text.

²⁹² *Nose to Nose—Boeing v. Airbus*, ECONOMIST (Special Report 2) (U.S. Ed.), June 25, 2005, at 69 (paraphrasing Harry Stonecipher, former Boeing chief executive).

²⁹³ *Id.*

company on a new design because of the enormous cost associated with developing an aircraft"²⁹⁴ Given the slim margin for error, a state-supported parachute is necessary when inventive risks fail, or else innovation is stifled.²⁹⁵ The SCM agreement is not practical as applied to the aircraft technology because it prohibits the funding that is necessary for greater innovation.

C. Discouraging Competition

The civil aircraft industry flies in the face of traditional *lassiez faire* economic thought. Generally, subsidies are thought to harm competition. Yet, with the commercial aviation industry, subsidies are necessary for competition.²⁹⁶

For the purpose of this comment, competition is assumed to be positive. The introduction of Airbus to the market should curb a recurrence of monopoly pricing that occurred with Boeing 747s during the 1970s, 1980s, and 1990s.²⁹⁷ Competition encourages competitive pricing, efficiency, and innovation. The SCM Agreement, however, keeps competitors out of the large civil aircraft market. The incredible financial burden in the industry requires government subsidies for a successful start-up period.²⁹⁸

²⁹⁴ Launius, *supra* note 31, at 64.

²⁹⁵ There is a one time bailout exception in the SCM Agreement. See *supra* note 135 and accompanying text. This, however, is not the type of continued support an aircraft manufacturer requires to be innovative.

²⁹⁶ See generally U.S. INT'L TRADE COMMISSION, COMPETITIVE ASSESSMENT OF THE U.S. LARGE CIVIL AIRCRAFT AEROSTRUCTURES INDUSTRY, USITC Pub. No. 3433 (June 2001) (on file with the North Carolina Journal of International Law and Commercial Regulation), available at <http://hotdocs.usitc.gov/docs/pubs/332/pub3433.pdf> (accessing the large civil aircraft industry's costs and different governments' involvement).

²⁹⁷ See WILL HUTTON, A DECLARATION OF INTERDEPENDENCE: WHY AMERICA SHOULD JOIN THE WORLD 232 (2004).

²⁹⁸ One author described the task of starting Airbus:

To design, build, and develop a fleet of state-of-the-art civil aircraft was always going to be a long-term task. It would require shareholders prepared to defer their returns for perhaps decades. It would require, as the American aerospace industry had received through defense contracts and tax rebates from export rates, billions of dollars of grants to support the public interest in possessing an aircraft manufacturer that the markets could not create spontaneously themselves. The time horizons for the returns on equity investment and private bank debt are extraordinarily short-term compared to the time needed to develop an aircraft business.

Introducing competitors into the large civil aircraft market is extremely difficult. It takes ten to twelve billion dollars just to get a new plane designed and ready for production.²⁹⁹ This sum does not even include the start-up costs for a manufacturing site. A manufacturer will recoup their investment in a new plane after selling 500-600 planes, or about ten years. The risks involved with starting up a commercial aircraft manufacturer are hard to stomach as a private investor. Governments and a limited number of large multinational corporations are the only entities capable of supporting such ventures. Further, to gain market share, prices must be cut; Airbus, for instance, was prepared to go through several unprofitable models before turning a profit.³⁰⁰

Considering the sacrifices necessary to gain part of the market share and the costly price tag to even compete in the market, it is not surprising that a government (or three or four) must be a forgiving creditor. Further, calculation of the interest rate must take into account the long period before the corporation becomes profitable. Jean Pierson, President of Airbus in 1987, explained in an interview: “[U.S. critics] were right to say that without money from the government at the time, when we were at zero we could never have beaten Boeing. What bank would have been stupid enough to have lent us money . . .”³⁰¹ Government loans that are used to start up an aviation giant are different than other loans; governments and other lenders cannot demand market level interest rates and repayment needs to be flexible. The SCM Agreement would characterize the tactics to start up Airbus as prohibited subsidization.³⁰² Essentially, the agreement, if followed, bars competitors from having a chance to enter the market.

D. Unrealistic

The world depends on commercial airplanes; it is unrealistic to expect the industry to not be subsidized. An estimated nine billion

Id. at 230.

²⁹⁹ *Id.*

³⁰⁰ See ARIS, *supra* note 16, at 160.

³⁰¹ *Id.*

³⁰² See discussion *supra* Part III.C.

global passengers board commercial airplanes each year.³⁰³ Despite the world's reliance on aviation, some calculations indicate that less than ten percent of commercial jets developed since 1982 have been profitable.³⁰⁴ As aerospace technology evolves it becomes more difficult for individual companies to bear the costs.³⁰⁵ A world without aircraft subsidies would result in the stagnation of innovation, at best. At worst, the price of flying would skyrocket and suffocate consumers.

Subsidies have built the commercial aviation industry. From European government support of aviation in the early twentieth century, to Cold War military contracts benefiting U.S. firms, to the Airbus consortium, the industry has greatly benefited from government aid. Antagonists may assert that aircraft subsidies create unfair competition. The irony is that every single aviation titan has been hoisted up by subsidies. Whether it is a corporation in Brazil, Canada, the United States, or the European Union, large civil aircraft manufacturers cannot exist without subsidies. The SCM Agreement, as applied to large civil aircraft, threatens the global industry.

E. Problems with the DSU

The DSU, relative to GATT and other previous trade agreements, is a significant innovation. Overall, many writers have had positive evaluations.³⁰⁶ Regardless, the system is still flawed. This comment asserts that the enforcement and compliance problems are aggravated when dealing with commercial aviation subsidies.

The DSU has already been widely criticized. The extent of this critique will be limited to the major flaw that is salient to the aviation dispute. The DSB has a difficult time enforcing its

³⁰³ See John Linder, *Prevent Terror Threats*, THE WASH. TIMES, May 30, 2005, at A23.

³⁰⁴ Levick, *supra* note 64, at 460-61.

³⁰⁵ See Launius, *supra* note 31, at 64.

³⁰⁶ As one commentator wrote, "the WTO dispute settlement system is a place where the United States and the European Communities can resolve their trade disputes though third-party adjudication and still conduct their trade relations effectively and responsibly, without the need for any special procedures." William J. Davey, *The WTO Dispute Settlement System: The First Ten Years*, 8 J. INT'L ECON. L. 17, 34 (2005).

recommendations and rulings when the stakes are high. In situations like the instant case, the DSU cannot produce an effective solution through litigation. There is a self-defeating loop created when both parties have committed similar violations. In this situation, compliance under the DSU is supposed to be compelled by a party who is also guilty of the same violation. This comment has asserted that all large civil aircraft producers have benefited from subsidization. Alleged subsidy violations, in regard to the civil aviation industry, will inevitably be defeated when both sides succeed with their claims. The SCM Agreement cannot be enforced under the DSU when applied to large civil aircraft.

As *EC—Bananas, U.S.—FSC*, and the Canada-Brazil aviation disputes have demonstrated, the DSU lacks a reliable compliance mechanism. While the DSU is an improvement over GATT, it has the same inherent problem of any international agreement—lack of enforcement.

The remedy for non-compliance under the DSU is self-help. This is problematic because it relies on the individual complainant to serve as an enforcer when a losing member resists a ruling. In disputes like the Canada-Brazil aircraft case where both sides are expected to be an enforcer, the agreement being subjected to litigation will not be upheld. It is in the best interest of both sides to refrain from engaging in a trade war. The result is non-compliance.

Consequently, the SCM Agreement is less likely to be enforced. The presence of a government subsidy is evidence that the State has an interest in that industry. When a member is devoted to maintaining non-compliant behavior, the DSU is unlikely to be effective. In instances like *U.S.—FSC*, the offending party can thwart compliance. Strong trade activity between members, like the United States and the European Union, discourage the use of authorized retaliation. This allows foot dragging and leads to no result from litigation.

VI. Forecasting the Future of the Skies

A. The possible avenues for the dispute

As of the writing of this comment, consultations have given

way to the panel stage.³⁰⁷ The avenues for the dispute are limited to either full litigation or a withdrawal of the claims.

WTO members prefer to negotiate and settle rather than litigate. At this point in the aviation dispute, an outside settlement would involve a withdrawal of the claims. In one academic's analysis of 181 disputes, the cases settled 35% of the time.³⁰⁸ Additionally, the matter was dropped 21% of the time due to commercial changes or the halting of a challenged matter.³⁰⁹ It appears as though the panel stage is reached only about half of the time after consultations are requested.³¹⁰ These statistics support the idea that settlement is preferred over litigation.

Public statements by the parties seem to indicate that a settlement is likely. Trade representatives for both sides have expressed their distaste for litigation and a preference for negotiation.³¹¹ The respective representatives for Boeing and Airbus have also voiced their hopes for a successful end with a settlement.³¹² Some believe, however, these public statements are just "posturing."³¹³

Even the DSU system encourages talking between the parties. The availability of DSB assistance through "good offices, conciliation and mediation"³¹⁴ is available at any time and assists in achieving a settlement.

Despite the signs pointing towards a settlement, full litigation seems inevitable. Barring major outside events rattling the aviation dispute, the panel and Appellate Body will likely get a chance to issue reports. The circumstances of the aviation feud have made it ripe for litigation.

First, the reason for requesting consultations and the panel in

³⁰⁷ WTO—Dispute Settlement—the disputes-DS317, http://www.wto.org/english/tratop_e/dispu_e/cases_e/ds317_e.htm (last updated Oct. 9, 2006).

³⁰⁸ *Id.* at 48.

³⁰⁹ *Id.*

³¹⁰ See *id.*; Mark Clough, *The WTO Dispute Settlement System—A Practitioner Perspective*, 24 FORDHAM INT'L L.J. 252, 264 (2000).

³¹¹ See *supra* note 171 and accompanying text.

³¹² See Ameet Sachdev, *Boeing Finance Chief Predicts Settlement on Subsidies*, CHI. TRIB., Oct. 14, 2005, §3, at 1.

³¹³ *Id.*

³¹⁴ See DSU, *supra* note 155, art. 5; WTO SECRETARIAT, *supra* note 156, at 94.

the first place was precisely because bilateral negotiations failed.³¹⁵ One may argue that litigation is part of a negotiation strategy, but if both parties really prefer to settle, a question remains: Why has neither side requested good offices, conciliation and mediation?

Second, a settlement would require concessions from both sides. This is why the dispute escalated to the DSB. On one hand, the United States has watched its civil aircraft dominance quickly evaporate. If the United States feels like it is reeling back on its heels it may be reluctant to allow any further government support for Airbus. On the other hand, Airbus is much more than just another corporation; for Europe it is a source of pride. It may be difficult to take Airbus off the former consortium's shoulders.

If the panel and appellate stages are not cut off by a settlement, then are three potential outcomes: (1) neither side winning, (2) one side prevailing, or (3) a two-sided victory.

Neither side prevailing is the least likely scenario. A reading of the respective evidence cited in the complaints in conjunction with the SCM Agreement suggests that both sides may be responsible for prohibited and actionable subsidization.³¹⁶

Only one party prevailing is also unlikely, given the evidence both sides have cited in their requests for consultations. If, however, there was a one-sided victory it would likely be in favor of the United States. This is because alleged EU subsidies are much more direct and easier to categorize as prohibited subsidies. Questionable loans to Airbus are characterized by the European Communities as "repayable loans," whereas the United States alleges this "launch aid" is either not paid back or set with interest below the market.³¹⁷ This does not take away from the lengthy list of tax breaks and research and design support that Boeing receives.³¹⁸ The United States may claim that the tax breaks are consistent with the benefits all other similar domestic industries

³¹⁵ See *supra* note 78 and accompanying text.

³¹⁶ See Consultation Request *EC—Aircraft*, *supra* note 2; Consultation Request *U.S.—Aircraft*, *supra* note 2; SCM Agreement, *supra* note 8.

³¹⁷ Editorial and Comment, *Unfair Skies: EU Subsidies to Airbus put U.S. Competitor at Significant Disadvantage*, COLUMBUS DISPATCH (Ohio), Sept. 28, 2005, at 12A.

³¹⁸ See Consultation Request *U.S.—Aircraft*, *supra* note 2.

enjoy. The US could argue that the taxes are not “otherwise due” and not a subsidy under the SCM Agreement. The U.S. subsidies appear to be much more like actionable, rather than prohibited, subsidies, which is a more flexible position to defend.³¹⁹ Regardless, the United States could run into trouble proving that government contracts with Boeing are not subsidies.

In the unlikely event that only one side emerges victorious, the dispute will likely drag on for decades. The instant dispute is a good candidate for full litigation with no result. The compliance problems featured in *EC—Bananas*³²⁰ and *U.S.—FSC*³²¹ could be employed by either side. The charade of compliance and foot dragging in *U.S.—FSC* would inevitably be used by a losing member. As *EC—Bananas* demonstrated, even half a decade of countervailing measures may not be enough to compel a loser to comply. Further, both sides are smart enough to realize that unleashing sanctions of this size could lead to a trade war with the entire global market as the loser. A one-sided victory would be most peculiar given the respective support the United States and European Union provide to Boeing and Airbus.

The most reasonable outcome would be a two-sided victory mirroring the Canadian-Brazilian aircraft dispute. This is not to suggest that any time two members file parallel complaints a dual victory will result. Rather, the U.S.-EU complaints appear to be equally compelling.

If both the United States and the European Union prevail, the outcome would be no result despite full litigation. Looking back at the Canada-Brazil aircraft dispute, after Canada and Brazil were awarded massive countervailing measures, both sides realized using them would be a lose-lose proposition. To date, the sanctions have not been imposed and the members simply continue to violate the SCM Agreement.³²² In the event of a dual victory, neither party has the incentive to comply with the DSB’s recommendations and rulings. An overly dramatic analogy would be a comparison to the cold war theory of mutually assured

³¹⁹ See *supra* Part III.D.

³²⁰ See *supra* notes 243-49 and accompanying text.

³²¹ See *supra* notes 252-61 and accompanying text.

³²² Edward Alden & Raphael Minder, *War of Aircraft Titans gives WTO Biggest Case*, FIN. TIMES (London), June 1, 2005, at 8.

destruction.³²³ In the event of non-compliance, arming the United States and European Union with multi-billion Euro countervailing measures is like handing over thermonuclear weapons. Partly out of fear of retaliation and the harm it would do to the world market, neither side would like to see a trade war. If this feud makes it through full litigation, it will likely have been a waste of time.

VII. Conclusion

So, what does this mean for the future of large civil aircraft and international trade? In the event of a settlement, or compliance after litigation, it would be a major mark of success for the WTO. Considering the instant dispute is thought to be the biggest case brought to the DSB, a successful resolution would add to the creditability of the DSU and the WTO overall.

Most likely, however, this dispute will serve as another footnote pointing to the shortcomings of the DSU. The circumstances have created a scenario that makes enforcement of the SCM Agreement unlikely. Both sides are likely to be found guilty of subsidization and neither side has a great incentive to give up its practices. The self-help trade sanctions made available as an enforcement mechanism have dubious utility in this dispute.

Despite the amount of attention the dispute has received, government support of the large civil aircraft industry will be maintained. If any changes are implemented, the aviation subsidies on both sides of the Atlantic will simply masquerade in different garbs. Any compliance will surely be token and subsidies will appear in different forms.

Finally, the SCM Agreement, as applied to large civil aircraft, is not pragmatic. Proponents of the agreement ignore the unique demands of the large civil aircraft industry. Halting subsidies to aviation manufacturers stifles innovation, handcuffs competition, and is unrealistic.

RYAN E. LEE

³²³ This is aptly abbreviated as MAD.

